ANNUAL REPORT ON THE DEVELOPMENT OF NATURAL GAS MARKETS IN ILLINOIS

ILLINOIS COMMERCE COMMISSION

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I. Introduction

This report fulfills the statutory requirement in Section 19-130, Commission Study and Report, of Article 19 (220 ILCS 5/19) of the Illinois Public Utilities Act ("Act"). Section 19-130 requires the Illinois Commerce Commission ("Commission") to prepare an annual report analyzing the status and development of the retail natural gas market in the State of Illinois, including data on volumes of natural gas sold to retail customers and the number of customers served by alternative gas suppliers and gas utilities. The required data is included in tables and attached as an appendix.

This report discusses the differences between traditional utility sales service and transportation service. Utility sales service constitutes the sale and delivery of natural gas supply to retail customers at regulated rates. The delivery component of utility sales service varies by customer class, but the tariffed rate for natural gas supply is the same for all customers. Transportation service allows multiple suppliers to sell competitively priced natural gas supply to retail customers. Customers that choose transportation service pay regulated utility rates for the delivery of natural gas but pay unregulated rates for natural gas purchased from alternative suppliers. Transportation service has the potential to result in lower prices, a wider array of services, and customized pricing, terms, and conditions of service for individual customers or groups of customers.

Transportation service has evolved from a simple to a more sophisticated service that offers customers a number of alternatives to traditional utility sales service. In 2003, transportation service accounted for approximately 41.3% of retail natural gas sales in Illinois. Most of this volume is attributable to large volume industrial and commercial customers served by more than 80 alternative retail suppliers. No alternative retail gas supplier served more than 5% of the market in 2003.

Transportation service is available to small commercial and residential customers in three utility service territories in Northern Illinois. The market for small volume customers is still evolving, but early signs of customer and supplier interest are encouraging. Overall, the number of transportation customers increased in 2003 by approximately 36,700, or 24%. The Gas Use Tax Law, the exiting of a major supplier, and other factors, may have contributed to a reduction in the number of large commercial and industrial customers on transportation service.

II. Bundled Utility Sales Service vs. Unbundled Gas Transportation Service

Shippers of natural gas, including gas utilities or Local Distribution Companies ("LDCs"), alternative gas suppliers, and other end-users, purchase gas supply at competitive prices from producing regions across North America and at various points along a vast network of federally-regulated interstate pipelines. Shippers must arrange for the delivery of natural gas to retail customers via interstate pipelines and state-regulated LDC distribution systems. LDCs take receipt of natural gas at points called "city gates", where their distribution systems connect with interstate pipelines. Large LDCs may be connected to multiple interstate pipelines with numerous city gates on each pipeline. Small LDCs may be connected to only one pipeline with fewer city gate connections. Once an LDC takes receipt of gas at a city gate, it becomes responsible for delivering that gas to retail customers connected to the LDC's system.

The Commission regulates thirteen Illinois LDCs with customer bases ranging in size from a few thousand customers to over 2 million customers. In Illinois, LDCs are required to offer "bundled", or sales, service to all retail customers on their system. Sales service customers pay a regulated rate that includes the cost of natural gas supply, intestate pipeline services, and local distribution service. Gas costs, including the price of natural gas supply, leased interstate pipeline services required to deliver the commodity to the LDCs system and hedging costs to moderate price swings in the gas market, flow through a Purchased Gas Adjustment Clause ("PGA"). Flowing the LDC's gas costs through the PGA results in a single PGA commodity price that is charged to all customers on utility sales service.

The Commission performs annual PGA prudence reviews to determine whether LDCs purchased gas in a prudent manner, and to reconcile the costs of delivered gas with the revenues collected from customers for that gas. The cost of prudently procured gas must equal the revenues received for that gas; otherwise, a surcharge or refund to customers is required. If an LDC’s gas purchases are deemed imprudent, the Commission disallows recovery of the imprudent costs associated with those purchases. PGA rates vary monthly to reflect the cost of gas that the LDC buys to meet the needs of sales service customers as a group.

All Illinois LDCs also offer transportation, or "unbundled", service to industrial and commercial customers as an alternative to sales service. Some Illinois LDCs offer transportation service specifically for small commercial and residential customers. Transportation service allows retail customers to purchase competitively-priced natural gas supply from alternative gas suppliers rather than price-regulated PGA gas from their LDC and offers customers the option to buy gas under terms that more closely reflect their individual needs. Alternative gas suppliers arrange for the delivery of transportation gas via interstate pipelines to the city gate or purchase supply at the city gate from wholesale suppliers. The LDC then takes receipt of that gas and delivers it to the suppliers' customers at a delivery rate that is regulated by the Commission.

The theory behind transportation service is that, unlike the delivery of gas, which requires regulation of natural monopoly infrastructure such as interstate pipelines and distribution networks, natural gas supply can be provided in a competitive market. Duplication of interstate pipelines and delivery system infrastructure would be uneconomical and would result in a higher cost of delivery service. On the other hand, allowing multiple shippers to sell natural gas supply to retail customers is expected to result in lower prices for natural gas supply, provide a broader offering of services that reflect the varying preferences of consumers, and allow suppliers to tailor pricing, terms, and conditions of service to better meet the needs of individual customers or niche markets.

Suppliers have offered a wide array of pricing options and other services to transportation customers. Offers have included fixed prices, market-based prices, market-based prices with the option to lock in a fixed price, market-based prices with a ceiling and a floor, discounts off of the LDC's PGA rate, and market-based prices in conjunction with a storage hedge. Suppliers have also offered discounts on gas service to customers that enroll via the Internet or telephone and discounts on other products and services.

III. History of Natural Gas Industry Restructuring in Illinois

A. ICC Advocacy of Open Access at the Federal Level

The ICC was an early supporter of the development of federal policies related to wholesale competition and the restructuring of the natural gas industry. With respect to the development and improvement of competitive wholesale markets, the ICC has focused most of its attention on key proceedings at the Federal Energy Regulatory Commission ("FERC"). Starting as far back as 1983, the Commission has intervened in numerous FERC proceedings to argue pro-competitive positions. The ICC has consistently argued before the FERC that competitive forces, where viable, will best protect the interests of consumers. Non-discriminatory interstate pipeline transportation is the crucial link between the competitive supply market and natural gas consumers.

B. Development of Retail Competition for Large Volume Customers in Illinois

For almost two decades, the ICC has been placing into effect unbundled gas transportation tariffs filed by Illinois LDCs. These LDC tariffs, in combination with interstate pipeline tariffs approved by the FERC, have created competitive supply markets for commercial and industrial customers. A sizable contingent of gas suppliers and marketers has developed to meet the needs of retail customers that choose to transport their own gas instead of purchasing PGA gas directly from their LDC under bundled tariffs. In 2003, transportation gas accounted for approximately 41.3 percent of all gas delivered to retail customers in Illinois -- a two percent decrease over last year. However, the number of customers on transportation service increased by approximately 18 percent from 199,504 to 236,195. The decrease in volumes transported and increase in number of transport customers is attributable to increased participation by residential customers and decreased participation by large volume commercial and industrial customers.

The ICC's approach toward retail competition in the natural gas industry has evolved over the past two decades to better reflect existing conditions in the industry. In the early stages of transportation service in Illinois, unbundled rate “design” amounted to simply deducting the PGA price from transported volumes. When transportation customers consumed LDC-supplied gas, they paid the regular PGA or bundled rate. Transportation rates have become more sophisticated over time as operating rules and charges have been developed to reflect the standby and balancing services provided to transportation customers. The charges are designed to recoup the cost of providing the level of firm LDC service requested by the customer. In addition, for customers that exceed their contracted level of firm gas service, there are various penalty charges or above-market rates that may apply. The purposes of penalty charges is to prevent large-scale imbalances beyond those that the LDC is prepared to accommodate pursuant to the terms and conditions and rates specified in the tariff and to protect against cross subsidization of transportation customers by bundled sales customers. Such penalties are often much more practical than the alternative of actually curtailing service to transportation customers whose gas supply does not reach the city gate—a clear advantage when customers number in the thousands as they do in the small volume transportation programs discussed below.

C. Small Volume Transportation Programs

An important recent development in Illinois retail natural gas markets is the introduction of small volume transportation programs, or "aggregation" programs, for small commercial and residential customers. Like large volume transportation programs, aggregation programs provide small volume customers with the opportunity to purchase competitively priced natural gas commodity from alternative retail gas suppliers as an alternative to traditional bundled utility service. Unlike large volume transportation programs, though, the cost of advanced metering that measures daily usage would render the service uneconomical for small volume customers. Instead of relying on advanced metering for measured daily usage, small volume transportation programs allow suppliers to aggregate customer load and rely on estimated daily usage of groups of customers for balancing purposes. Over the past seven years, the Commission has approved several small volume transportation pilot programs, some of which have developed into permanent programs. In December 2003, approximately 152,000 residential customers and 57,000 commercial customers were served under small volume transportation programs in Illinois.

1. Peoples Gas Light and Coke Company's and North Shore Gas Company’s “Choices For You” Programs

On May 15, 1997, Peoples Gas Light and Coke Company (“Peoples”) filed small volume transportation tariffs, which would later become known as the “Choices For You” program. These tariffs went into effect on June 29, 1997, and Peoples implemented a two-year pilot transportation program for small volume commercial customers that would expire in October 1999.

In April 1999, the Commission granted an extension of the Pilot Program through June 2000. On May 9, 2000, Peoples proposed to eliminate the termination date of the program and implement other revisions to the tariffs, such as amending the restrictions placed on the number of customers that can be aggregated into one group, increasing the number of eligible customers, making the program available to more suppliers, reducing certain fees and charges, altering the methods used to determine the scheduling of nominations and storage injections and withdrawals, modifying some of the supplier participation requirements, and amending the customer sign-up, billing and enrollment processes. On June 30, 2000, the Commission approved Peoples' filing to place into effect a permanent unbundling program for all non-residential customers with an annual consumption of less than 50,000 therms.

On May 16, 2001, Peoples filed to revise its "Choices For You" program and allow for residential customers to participate on a limited basis. On March 5, 2002, the Commission issued its Final Orders allowing Peoples and North Shore to move forward with their plans to phase in residential transportation service on a pilot basis over a period from May 1, 2002 through April 30, 2005. Table A contains the participation limits set by the Commission for residential customers.

Table A – Residential Participation Limits by Service Territory		
Period	**Peoples**	**North Shore**
May 1, 2002 through April 30, 2003	98,000	18,000
May 1, 2003 through April 30, 2004	181,000	33,000
May 1, 2004 through April 30, 2005	249,000	45,000

The participation limits are a function of the number of residential customers in each company's service territory. On or before October 1, 2004, the companies are required to file participation limits for April 30, 2005 and beyond. The enrollment limits have not prevented customers from participating as the limits far exceed current enrollment levels.

2. Nicor's "Customer Select" Program

In October of 1997, the Commission approved Nicor's filing to place into effect Rider 15, Customer Select Pilot Program, Rider 16, Supplier Aggregation Service, and some proposed revisions to existing tariff sheets. The combination of these tariffs allowed Nicor to offer a pilot transportation program to small volume industrial and commercial customers that had not found service under existing transportation tariffs to be economical.

In September 1998, Nicor received Commission approval to expand availability of the program to a total of approximately 65,000 industrial and commercial customers and 80,000 residential customers. The second year of "Customer Select" commenced on May 1, 1999, and marked the first time that residential customers in Nicor's service territory were allowed to choose their own natural gas supplier.

In September 1999, Nicor received Commission approval to expand availability of the Customer Select program to a total of 265,000 residential customers and all commercial and industrial customers. The third year of the “Customer Select” pilot program began on May 1, 2000. On August 11, 2000, the Company filed to transform the pilot program into a permanent program available to approximately 1.9 million customers. On September 20, 2000, the Commission suspended the filing and commenced an investigation into Nicor’s proposed permanent “Customer Select” program.

On July 6, 2001, the Commission issued its Final Order, allowing Nicor to move forward with a permanent “Customer Select” program. On March 1, 2002, “Customer Select” became available to all of the nearly 2 million residential, commercial, and industrial customers in Nicor’s service territory.

3. Central Illinois Light Company's Small Volume Transportation Program

In 1996, Central Illinois Light Company ("CILCO") filed the first pilot residential unbundling program in the State of Illinois. While there was some initial interest from suppliers and customers, suppliers eventually withdrew from the program. The lack of supplier interest may have been associated with high marketing costs per customer given the limited size of the program. The pilot phase was scheduled for five years. CILCO's pilot residential unbundling program expired in 2001 and is no longer available.

IV. Value of Unbundled Service to Small Volume Customers

Supplier offerings differ in several ways from the PGA charges that LDCs assess to sales service customers. The PGA reflects the Company’s actual cost of gas. To the extent that the Company’s commodity costs fluctuate with the market, the PGA also fluctuates with the market. As mentioned in Section II above, suppliers have offered a wide array of pricing options and other services to small volume transportation customers.

Program benefits depend on the prices and services offered by each supplier and the value that each customer derives from their chosen service option. For example, if a customer enters into a fixed price contract with a supplier, the customer could be better off or worse off depending on the direction that market prices follow after the fixed price contract is effectuated. Even if a customer enters into a fixed price contract and gas prices subsequently drop below the level of the fixed price, it cannot unequivocally be argued that the customer was harmed by the fixed price contract. This is because there is a benefit, albeit a benefit that is difficult to place a dollar value on, to eliminating the uncertainty associated with the PGA charge or any other variable price.

While it cannot be unambiguously said that small volume customers taking service under the programs have benefited, the popularity of the programs indicates a belief by small volume customers that they derive benefits from the option to choose alternative gas suppliers. Nearly 210,000 customers participated in the programs in calendar year 2003, an overall 24% increase in participation. Table B shows data for Nicor's, Peoples', and North Shore's small volume transportation programs as of December 2003 and December 2002, respectively.

Table B - Small Volume Transportation Customers by LDC						
	Residential		Commercial		Total	
Program	2002	2003	2002	2003	2002	2003
Nicor - Customer Select	100,632	145,072	50,741	48,864	151,373	193,936
Peoples - Choices For You	6,122	3,973	9,789	8,261	15,911	12,234
North Shore - Choices For You	1,364	2,804	301	353	1,665	3,157
Total	**108,118**	**151,849**	**60,831**	**57,478**	**168,949**	**209,327**

While these programs are still evolving, the data nevertheless provides evidence that small volume residential and commercial customers will participate in competitive markets where aggregation tariffs are available. As mentioned above, Nicor's program has only been available on a permanent basis to all customers in Nicor's service territory since March 1, 2002. Peoples' and North Shore's small volume transportation programs became available on a pilot basis to a limited number of residential customers for the first time beginning on May 1, 2002. Because Nicor's, Peoples', and North Shore's small volume transportation programs have only been available on either a permanent or pilot basis for less than two years as of December 2003, it would be premature to make an assessment on the level of competition for residential and small volume commercial customers in these service territories. However, early participation rates and supplier interest have been encouraging, particularly in Nicor's service territory.

The growth in customer participation was largely driven by a 44% increase in residential customer participation in Nicor's service territory. Participation by commercial customers in Nicor's service territory fell by 3.7%. The decline in commercial customer participation is attributable to several factors including the dissolution of Nicor Energy L.L.C. and the implementation of the Gas Use Tax Law. Overall participation in Nicor's Customer Select grew by approximately 28%.

Overall participation in Peoples' Choices For You fell by 23%. Residential participation fell by 35%, and small volume commercial customer participation fell by 15%. Although the percentage of eligible customers participating is relatively low, overall participation in North Shore's Choices For You increased by 89%. Residential participation in North Shore's Choices For You increased by 105%, and small volume commercial customer participation increased by 17%.

The lack of participation in Peoples' Choices For You is attributable to several factors. First, Nicor Energy L.L.C was a major supplier in Peoples' service territory.

Nicor Energy L.L.C disbanded in early 2003 and is no longer in business. Nicor Energy L.L.C.'s former customers faced with taking service from one of two remaining suppliers or returning to utility sales service. Some chose to return to utility sales service. Second, the Gas Use Tax Law raised the cost of transporting gas by approximately 2.4 cents per therm. Third, only two suppliers are currently marketing to residential and small commercial customers in Peoples' service territory.

Certified suppliers have focused their marketing efforts on customers in Nicor's service territory rather than Peoples' service territory for a number of reasons, including program permanence, rate structures, and eligibility. Nicor's Customer Select is a permanent program – a market that suppliers will be able to tap into the foreseeable future with certainty. In contrast, the residential portion of Peoples' Choices For You is a pilot program. Peoples has not yet filed to make Choices For You a permanent program for residential customers but is required to make a filing that will address availability of the program going forward by October 1, 2004. So, uncertainty over the future of Peoples' program still exists.

The cost of signing up new customers is greater in Peoples' service territory than in Nicor's service territory. Peoples assesses a $10 charge for signing up new customers. Nicor only charges a $10 fee when suppliers sign-up customers that have previously taken service under Customer Select. There is no charge when suppliers sign-up customers on utility sales service that have yet to participate in Customer Select.

In addition to the permanence of Nicor's program, more customers are eligible for transportation service in Nicor's service territory. Not only does Nicor's service territory have over twice as many customers as Peoples' service territory, there is no participation limit in Nicor's service territory. Peoples' Choices For You tariff limited participation to 181,000 residential customers for the 2003/2004 winter heating season and North Shore's tariff limited participation to 33,000 residential customers for the same period. In contrast, Nicor's Customer Select is available to approximately 2 million residential customers. It may appear as if the participation limits in Peoples' and North Shore's service territories are not an issue because actual participation is nowhere near the limit in either service territory. However, the low level of customer participation may partially attributable to the existence of participation limits. Participation limits represent a maximum number of customers that can be served if one or more suppliers focus there marketing efforts on the limited service territories. Because there are economies of scale in serving residential customers, suppliers focus their marketing efforts where a greater number of customers can be served. This results in a lower level of marketing to residential customers in service territories with participation limits and limits the number of available alternatives to sales service.

The permanence of Nicor's program, the greater number of eligible residential and commercial customers, the absence of any participation limitation on residential customers, and the lack of a switching fee when customers switch from utility service, all create a more attractive market in Nicor's service territory. This is reflected not only by the number of participating residential customers but also by the number of suppliers marketing to small volume customers in each service territory. Nicor's Customer Select has eight actively participating suppliers while Peoples and North Shore's Choices For You have only two participating suppliers.

As suppliers become more familiar with small volume markets in Northern Illinois, customers become more familiar with unbundled gas service, and small volume transportation programs are refined, the Commission expects that participation in competitive markets by small volume customers will expand. Increased supplier and customer participation, specifically, in Nicor's service territory are encouraging signs.

V. Recent Developments in Retail Natural Gas Markets

A. AmerenCIPS and AmerenUE Group Balancing Service

On October 22, 2003, the Commission issued a Final Order in Docket Nos. 02-0798/03-0008/03-0009 (Consolidated), AmerenCIPS' and AmerenUE's (collectively "Ameren") Proposed General Increases in Natural Gas Rates. During the course of the proceeding, Ameren agreed to proposals by Commission Staff and intervenors to implement a group balancing service for commercial and industrial customers in the CIPS and UE service territories. The parties also agreed that the tariff should be effective for the winter of 2004. The Commission's Final Order required the parties to hold workshops to define and develop the terms and conditions for a group balancing service, subject to Commission approval.

Group Balancing allows suppliers or agents representing multiple transportation customers to group together customers' accounts when nominating gas to the utility's delivery system, managing customers' storage accounts, and balancing deliveries with usage. Group balancing is expected to reduce transaction costs associated with managing multiple transportation customer accounts and reduce the level of penalty charges assessed to transportation customers without impacting utility service. Under AmerenCIPS and Ameren UE's current tariff conditions, suppliers, acting as agents for transportation customers, are required to schedule separate deliveries for each transportation customer and balance each customers account individually. This requires both the utility and the supplier to track activity for each transportation customer on an individual account basis. Ameren's group balancing service will be available to commercial and industrial customers with metering devices that measure daily usage.

In anticipation of the workshop process, Ameren consulted with Staff and drafted tariff provisions, to implement a group balancing service. The draft tariff conditions were circulated to interested parties for review. A workshop was held on February

10, 2004, in Springfield. Representatives from Commission Staff, Ameren, suppliers, and other interested parties attended the workshop and provided input on the draft tariff conditions. A general consensus was reached at the workshop, and Ameren is now in the process of finalizing a proposed group balancing service to file for Commission review.

B. Peoples Storage Collaborative

North Shore, Peoples, ICC Staff, and various suppliers participated in a Commission-ordered collaborative process in order to facilitate a more efficient use of storage for Choices For You customers. The majority of Choices For You customers use natural gas for heating purposes. At issue was the manner in which gas was withdrawn from storage during the winter heating season to serve Choices For You customers. Gas was withdrawn from storage in equal amounts on each day during a given month. This required suppliers serving “Choices For You” customers to absorb daily fluctuations in demand through changes in deliveries to the Company’s system. The collaborative process resulted in a storage plan that absorbs some demand fluctuation through storage withdrawals, rather than pipeline deliveries, by linking storage withdrawals to temperature. When a consensus was reached among the workshop participants, Peoples filed a new storage withdrawal plan, which was approved by the Commission and implemented for the 2003/2004 heating season.

C. Nicor Energy L.L.C. Exits the Market

Nicor Energy L.L.C. was a joint venture between Nicor Inc. (the parent company of Nicor Gas Company) and Dynegy Inc. that offered natural gas, electricity, and energy-related services to industrial commercial and residential customers in the Midwest. In February 2003, Dynegy and Nicor Inc. began to dismantle their jointly owned Nicor Energy L.L.C. unit by selling approximately 132,000 retail natural gas customer accounts to Dominion Retail, a division of Richmond, Virginia-based Dominion Resources Inc. The majority of these accounts were residential and small commercial customers in Nicor’s “Customer Select” program, although the sale also included some residential and small commercial accounts in Peoples’ “Choices For You” program.

In March 2003, Nicor Energy L.L.C. turned its focus to selling its larger commercial and industrial accounts. On March 27, 2003, Accent Energy Group L.L.C. announced the acquisition of approximately 1,700 commercial and industrial accounts across northern Illinois from Nicor Energy L.L.C. Nicor Energy L.L.C. reported that the transaction completed its efforts to assign all of its existing contracts for retail energy supply to qualified energy suppliers.

The acquisition and transfer of customer accounts from Nicor Energy L.L.C. to other competitors have been relatively smooth. Customers were not required to take any action as a result of the reassignment of their contracts. Both acquiring suppliers pledged to honor the terms and conditions of the acquired contracts.

D. Article XIX – Alternative Gas Supplier Law

Article 19, “Alternative Gas Supplier Law” (220 ILCS 5/19), of the Act requires the Commission to adopt rules through which it will certify all alternative gas suppliers that serve or seek to serve residential natural gas customers and commercial customers with an annual usage of 5,000 therms or less. Illinois Administrative Code Part ("Code Part") 551 details the financial, managerial, and technical requirements that alternative gas suppliers must meet in order to be certified. Amendments to Code Part 551, which included certification requirements for suppliers serving small commercial customers and other consumer protections, were put into effect in January 2004.

The Commission has certified ten suppliers under Article 19 of the Act. In addition, the Staff of the Commission is handling a steady flow of inquiries from suppliers that are interested in being certified to serve residential and small commercial customers in Illinois. The following suppliers are currently certified to serve residential customers in Illinois: Corn Belt Energy Corporation, Dominion Retail Inc., Interstate Gas Supply of Illinois, Inc., MX Energy Inc., Peoples Energy Services Corporation, Santanna Energy Services, Shell Energy Services Company, LLC., U.S. Energy Savings Corp., and Utility Resource Solutions L.P.

E. Gas Use Tax Law

Changes in taxes on natural gas usage have reduced the incentive to transport gas for customers who had not transported gas before March 1995. On June 20, 2003, Governor Blagojevich signed SB1733, creating Article 5, "Gas Use Tax Law" (Public Act 93-0031). The Gas Use Tax Law assesses a tax of either 2.4 cents per therm or 5% of the purchase price of natural gas to transportation customers, depending on the tax payment method that the customer selects. The tax went into effect on October 1, 2003. Use of gas by the following entities is exempt from the tax: governmental bodies, charitable, religious and educational organizations, gas-fired electric generators, petroleum refineries, anhydrous ammonia and downstream nitrogen fertilizer producers, and producers of natural gas byproducts for resale.

The Gas Revenue Tax Act (35 ILCS 615) assesses a similar tax on gas consumed by sales service customers. However, any customer that had taken transportation service on or before March 1, 1995, was exempted from the tax on sales service under the Gas Revenue Tax Act. Exempted customers were able to switch to sales service without being taxed under the Gas Revenue Tax Act. Sales service customers that had not taken transportation service prior to March 1, 1995 could avoid the Gas Revenue Tax by switching to transportation service.

The Gas Use Tax Law amended the Gas Revenue Tax Act to eliminate the tax advantage of being on transportation service for all customers. So, those customers that were exempted from the Gas Revenue Tax on sales service now face a similar, but heretofore not incurred tax, regardless of whether they choose sales or transportation service.

The post 1995 transportation customers were subject to the Gas Revenue Tax if they were to switch to sales service. For those customers, the Gas Use Tax Law increased the cost of transportation service relative to sales service and, all other things equal, provided an incentive to switch back to sales service. Some of these customers presumably migrated back to sales service when the tax advantage was eliminated. For example, part of the decline in commercial customer participation in Nicor's and Peoples' small volume transportation programs can be attributed to the Gas Use Tax Law. It is difficult to gauge the overall impact of the tax on transportation service in Illinois because the data does not reveal which specific transportation customers were exempt from the Gas Revenue Tax Act. However, despite the increased cost of transportation gas due to the new tax, small volume commercial and residential customers continue to find value in gas transportation. The majority of these customers were not transportation customers prior to March 1, 1995.

VI. 2003 Calendar Year Data, Summary and Conclusions

Section 19-130, Commission Study and Report, of Article 19 (220 ILCS 5/19) of the Act requires this report to include the following data:

> (1) the aggregate annual demand of retail natural gas customers in the State of Illinois in the preceding calendar year;
>
> (2) the total annual therms delivered and sold to retail customers in the State of Illinois by each gas utility and each alternative gas supplier in the preceding calendar year;
>
> (3) the percentage of therms delivered and sold to customers in the State of Illinois in the preceding calendar year by each gas utility and each alternative gas supplier;
>
> (4) the total number of customers in the State of Illinois served in the preceding calendar year by each gas utility and each alternative gas supplier;

Appendix A attached to this document provides the data required in Section 19-130. Gathering accurate data to include in this report remains problematic. Utilities, however, were better prepared to provide the required information this year as compared to last year (the first year that the report was required to be filed). In the past, utilities have not closely tracked which parties have title to gas that is nominated to their distribution systems. Most transportation customers have a designated agent that acts as a liaison between the utility and the transportation customer. This agent may be an alternative gas supplier as defined in Section 19-105 of the Act, or the agent may be a consultant that arranges for an alternative gas supplier to deliver gas to the city gate on behalf of one or more transportation customers. The latter never takes title to the gas and, therefore, does not offer gas for sale, lease, or in exchange for other value received to one or more customers or engage in the furnishing of gas to one or more customers. Rather, the entity essentially acts as a gas-purchasing consultant. This year, utilities better differentiated between actual alternative gas suppliers as defined in Section 19-105 and agents that represented customers but never took title to gas delivered to the utilities' system.

Other problems that arose last year continue to be prevalent in the data provided for this year's report. In many cases, the utilities failed to provide proper or updated legal names of suppliers, resulting in the same suppliers being listed several times under different names. Wholesale supplier activity was reported as retail supplier activity. Some customers do not have a designated agent and purchase gas from a different supplier each month. Complicating matters further, most suppliers serve large volume customers and, hence, are not certified by the Commission. These suppliers are under no obligation to verify data provided by the utility and most consider the data proprietary. Therefore, individual suppliers are not identified.

Although questions remain about the accuracy of the data supplied by gas utilities, any inconsistencies in the data will not have a significant impact on market share because the identities of the largest suppliers have been verified. While information on individual suppliers may not be perfectly accurate, the data does provide insight into the level of retail competition in the natural gas industry.

The aggregate annual demand of Illinois retail natural gas customers in 2003 was approximately 9.2 billion therms. More than 236,000 transportation customers purchased nearly 42% of the total gas sold to Illinois retail customers from more than 80 alternative retail gas suppliers. The remaining 58% was delivered by Illinois LDCs and sold at regulated PGA rates to more than 3.7 million Illinois retail natural gas customers. The greatest market share among alternative gas suppliers was 4.7% of the total volumes delivered to both transportation and sales service customers. No other alternative gas supplier had greater than a 4% market share in 2003. The number of participating suppliers and low supplier market shares reflect a significant level of statewide retail competition, especially for large volume customers, which account for the majority of transportation volumes in Illinois.

Section 19-130 requires that market share data, based on the total number of therms delivered and sold to all retail customers in Illinois (sales service and transportation), be included in this report. **Data measuring each supplier's market share of the transportation market only**, rather than the entire Illinois retail market, provides a different perspective on the level of competition by focusing on competition between alternative gas suppliers rather than the broader measure of total deliveries that includes both utility bundled sales and alternative gas supplier sales. Table C shows the 2003 top ten suppliers' market share of transportation volumes in 2003, market share of transportation volumes in 2002, and their 2002 market share ranking. A comparison of 2003 and 2002 numbers shows some stability in the total share of the top ten producers. The top ten suppliers served 55.6% of the transportation market in 2003. In 2002, the top ten suppliers served 56.2% of the market. While eight of the top ten suppliers in 2003 were also in the top ten in 2002, two major changes occurred among the firms. First, the largest supplier in 2002 became the fourth largest supplier in 2003 and its market share dropped over ten percentage points. With this drop the share of the largest supplier dropped from 15.7% to 11.3%. Second, a small marketer in 2002 jumped to the fifth position raising it market share almost 5 percentage points. The remainder of the suppliers either stayed in the same position or shifted only slightly in their rankings. Overall, the level of market concentration remained low in 2003 reflecting a market where a significant level of competition exists.

Table C - Market Shares and Rank of 2003 Top Ten Suppliers in 2002

Top Ten Suppliers in 2003	Rank of 2003 Top Ten Suppliers in 2002	Market Share of Transportation Volumes in 2003	Market Share of Transportation Volumes in 2002
1	2	11.3%	9.4%
2	4	9.4%	6.9%
3	3	8.3%	7.5%
4	1	5.1%	15.7%
5	49	4.7%	0.1%
6	6	4.2%	4.9%
7	7	3.4%	4.4%
8	10	3.2%	2.5%
9	9	3.2%	2.7%
10	13	2.8%	2.1%

A significant number of large volume commercial and industrial customers switched from transportation to sales service in 2003. In 2002, 30,555 large volume commercial and industrial customers took service under traditional transportation tariffs. In 2003, the number of large volume commercial and industrial customers on traditional transportation tariffs declined to 26,868. This migration to sales service is likely due to a number of factors including: the dismantling of one of the largest suppliers in the state, the impact of the Gas Use Tax Law, economic conditions and other concerns about deregulated energy markets.

With more residential customers eligible for transportation service and more suppliers targeting Illinois markets, the number of customers taking transportation service continues to rise. Large volume commercial and industrial customers may re-enter the market as new suppliers fill the void left by the exit of Nicor Energy

L.L.C., the impact of the Gas Use Tax Law is fully realized, and economic conditions make transportation service more attractive.

Section 19-130 - Natural Gas Utility Sales and Transoprtation Data - Appendix A

Subtotal - Utility Bundled Sales Service	**5,382,299,055**
Subtotal - Alternative Gas Suppliers	**3,791,527,012**
Total Retail Sales - 2003	**9,173,826,067**

Utility - Bundled Sales Service	Annual Therms Delivered and Sold in 2003	Number of Customers Served in 2003	Percentage of Total Therms Delivered and Sold in 2003
Nicor Gas Company - Utility	2,685,971,195	1,867,022	29.28%
Peoples Gas Light & Coke Company - Utility	1,248,204,380	796,549	13.61%
Illinois Power Company - Utility	553,892,271	415,702	6.04%
Central Illinois Light Company - Utility	264,277,710	209,510	2.88%
North Shore Gas Company - Utility	261,187,020	149,226	2.85%
Central Illinois Public Service Company - Utility	198,009,970	171,601	2.16%
MidAmerican Energy Company - Utility	81,748,555	64,924	0.89%
Atmos Energy - Utility	36,008,260	23,547	0.39%
Union Electric Company - Utility	23,265,680	18,229	0.25%
Illinois Gas Company - Utility	12,765,646	10,258	0.14%
South Beloit Water Gas and Electric Company - Utility	9,244,962	7,302	0.10%
Interstate Power and Light Company - Utility	7,247,048	5,540	0.08%
Mount Carmel Public Utility Company - Utility	476,358	3,687	0.01%
Subtotal - Utility Bundled Sales Service	**5,382,299,055**	**3,743,097**	**58.67%**

Alternative Gas Supplier	Annual Therms Delivered and Sold in 2003	Number of Customers Served in 2003	Percentage of Total Therms Delivered and Sold in 2003
1	429,862,554	24,500	4.69%
Transport w/out Designated Supplier	386,113,309	37	4.21%
2	356,512,523	176	3.89%
3	315,235,948	6,216	3.44%
4	192,689,430	1	2.10%
5	178,638,055	110,518	1.95%
6	158,881,050	717	1.73%
7	130,728,949	2,138	1.43%
8	121,851,130	824	1.33%
9	119,495,429	28,340	1.30%
10	106,465,749	1,147	1.16%
11	105,686,151	1,020	1.15%
12	95,805,895	699	1.04%
13	77,303,037	292	0.84%
14	72,186,922	1,236	0.79%
15	71,433,247	13	0.78%
16	66,007,376	1,654	0.72%
17	59,921,569	1	0.65%
18	51,169,191	97	0.56%
19	47,940,591	17	0.52%
20	45,681,954	221	0.50%

Section 19-130 - Natural Gas Utility Sales and Transoprtation Data - Appendix A

Alternative Gas Supplier	Annual Therms Delivered and Sold in 2003	Number of Customers Served in 2003	Percentage of Total Therms Delivered and Sold in 2003
21	42,429,167	102	0.46%
22	40,385,995	17	0.44%
23	38,249,717	1,408	0.42%
24	37,001,696	42	0.40%
25	36,221,377	551	0.39%
26	32,184,647	238	0.35%
27	30,657,043	1	0.33%
28	30,103,022	20	0.33%
29	29,976,719	118	0.33%
30	29,781,166	49,038	0.32%
31	25,648,409	178	0.28%
32	22,429,976	15	0.24%
33	22,228,530	5	0.24%
34	17,945,941	-	0.20%
35	14,633,433	151	0.16%
36	11,864,279	5	0.13%
37	9,973,462	79	0.11%
38	8,968,611	6	0.10%
39	8,693,497	239	0.09%
40	8,148,487	46	0.09%
41	7,914,394	1	0.09%
42	7,716,916	3	0.08%
43	6,941,960	325	0.08%
44	6,347,100	17	0.07%
45	6,085,908	1	0.07%
46	5,780,577	21	0.06%
47	5,520,774	393	0.06%
48	4,428,979	-	0.05%
49	4,339,810	4	0.05%
50	4,118,783	2,496	0.04%
51	3,623,220	107	0.04%
52	3,368,414	215	0.04%
53	3,354,953	14	0.04%
54	2,908,556	2	0.03%
55	2,835,393	33	0.03%
56	2,715,341	272	0.03%
57	2,713,190	2	0.03%
58	2,659,124	2	0.03%
59	2,642,809	7	0.03%
60	2,072,783	3	0.02%
61	1,961,829	1	0.02%
62	1,824,499	1	0.02%
63	1,271,186	5	0.01%
64	1,206,542	2	0.01%

Section 19-130 - Natural Gas Utility Sales and Transoprtation Data - Appendix A

Alternative Gas Supplier	Annual Therms Delivered and Sold in 2003	Number of Customers Served in 2003	Percentage of Total Therms Delivered and Sold in 2003
65	1,161,481	1	0.01%
66	1,043,990	1	0.01%
67	1,003,648	1	0.01%
68	906,989	3	0.01%
69	898,018	2	0.01%
70	785,730	6	0.01%
71	769,562	25	0.01%
72	762,575	43	0.01%
73	735,700	3	0.01%
74	699,039	-	0.01%
75	478,478	15	0.01%
76	305,688	1	0.00%
77	173,996	13	0.00%
78	102,390	1	0.00%
79	100,660	3	0.00%
80	99,414	1	0.00%
81	11,381	26	0.00%
Subtotal - Alternative Gas Suppliers	**3,791,527,012**	**236,195**	**41.33%**